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In the Supreme Court of the United States

OCTOBER TERM, 1933

No. —

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, petitioner

v.

SUSAN DWIGHT BLISS

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

The Solicitor General, on behalf of the Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the Circuit Court of Appeals for the Second Circuit entered in the above cause on January 15, 1934, reversing the decision of the Board of Tax Appeals. (R. 31.)

OPINIONS BELOW

The findings of fact and opinion of the Board of Tax Appeals (R. 16–20) are reported in 27 B.T.A. 205. The opinion of the Circuit Court of Appeals for the Second Circuit (R. 26) is not yet reported.

QUESTION PRESENTED

Where the taxpayer elects to be taxed under Section 101 (a) of the Revenue Act of 1928, does the basis for computing the 15% deduction allowable for contributions under Section 23 (n) of the Act include capital net gains or ordinary net income only?

STATUTES INVOLVED

The statutes involved are set forth in the Appendix, *infra,* pp. 9–12.

STATEMENT

This is a proceeding for the redetermination of deficiencies in income taxes for the years 1928 and 1929. It was begun by notice of deficiency sent to the taxpayer by the Commissioner of Internal Revenue relating to certain deductions not here material. (R. 2, 9.) By amended answers to the taxpayer's petitions to the Board of Tax Appeals, the Commissioner set forth as an additional ground for assessment of deficiencies that the taxpayer, having elected to be taxed under Section 101 (a) of the Revenue Act of 1928, had claimed deductions for charitable contributions in excess of the 15% of her new income allowed by Section 23 (n) of the Act. (R. 7–8, 12–13.)

The facts were stipulated, and as so stipulated may be summarized as follows (R. 13–15):

The amount of charitable and other contributions made by the taxpayer during the years 1928 and 1929 of a character deductible from net income sub-

ject to the limitations provided in Section 23 (n) of the Revenue Act of 1928 (*infra,* p. 10), was $43,995.92 (R. 14) for the year 1928, and $39,088.46 for the year 1929 (R. 15). The ordinary net income of the taxpayer before deducting the amounts of such contributions was $270,490.77 for the year 1928 (R. 14) and $247,571.83 for the year 1929 (R. 15). The taxpayer's capital net gain for 1928 was $211,544.82 (R. 14), and for 1929 was $299,942.31 (R. 15).

The taxpayer deducted the respective total amounts of the charitable and other contributions from the respective years' gross income upon the ground that in determining the 15% limitation for charitable deductions under Section 23 (n) of the 1928 Act (*infra,* p. 10) ordinary income and capital net gains should both be included, regardless of her election to be taxed under Section 101 (a) of the Act.

The Commissioner took the position that deductions for contributions should be limited to 15% of the "ordinary net income," excluding "capital net gains" by virtue of the election to be taxed under Section 101 (a). (R. 8, 12–13.) In this he was sustained by the Board of Tax Appeals. (R. 19.) The Circuit Court of Appeals reversed, Judge Learned Hand dissenting. (R. 26–31.)

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In including the taxpayer's capital net gain for the calendar years 1928 and 1929 in computing

the 15% limitation upon contributions deductible from the taxpayer's gross income for those years, pursuant to Section 23 (n) of the Revenue Act of 1928.

2. In reversing the Board of Tax Appeals.

REASONS FOR GRANTING THE WRIT

1. The court below has decided a question of general public importance which should be settled by this Court.

The taxpayer elected to have her capital net gains taxed under Section 101 (a) of the 1928 Act (*infra*, p. 10) rather than in the normal manner. Under that section the taxpayer is given the option of having his capital net gain segregated from his ordinary net income and taxed at a flat 12½% rate. Where a taxpayer elects to be taxed under Section 101 (a) his total net income is divided into two separate classes: capital net gains and "ordinary net income". These two classes are computed separately and taxed separately at different rates. When this election is exercised, it was the intent of Congress that the two types of income should be completely segregated and that items coming within one class should not influence the computation of the tax on the other class. The 15% limitation for contribution deductions (which are ordinary deductions under Section 101 (c) (4) (*infra*, p. 11), should consequently not be affected by capital net gains. This purpose of segregation is clearly evidenced by the language of Section 101 (a) (b) and (c) (*infra*, pp. 10–11).

The Treasury Department advises that there are pending in the courts, before the Board of Tax Appeals, and in the Income Tax Unit of the Bureau of Internal Revenue 388 cases involving taxes in the total amount of $2,597,993.02, dependent entirely upon the determination of the question here involved.[1] These figures are entirely exclusive of cases pending in the field. It is known that there are a great many of such cases but it is impossible to estimate either the number or the amount involved.

Moreover, since the statutes here involved appear in all the Revenue Acts from 1921 to 1932, inclusive, the question is one of present importance and it will

[1] Several of these cases have reached the courts. Aside from *Helvering* v. *Harbison*, No. —, October Term, 1933, and *Helvering* v. *Colgate*, No. —, October Term, 1933, petitions for writs of certiorari in which cases are filed simultaneously herewith, one other case has been decided by a Circuit Court of Appeals, contrary to the Commissioner's contention. *White* v. *Atkins*, C.C.A. 1st, decided March 14, 1934, with one judge dissenting, affirming *Atkins* v. *White*, 3. F. Supp. 694 (D. Mass.). The following cases are pending in the various Circuit Courts of Appeals:

Straus v. *Commissioner*, 27 B.T.A. 1116, now pending after argument in the Court of Appeals of the District of Columbia; *Robinette* v. *Commissioner*, 27 B.T.A. 1426, now pending before argument in the Circuit Court of Appeals for the Third Circuit; *Igleheart* v. *Commissioner*, 27 B.T.A. 1426, now pending after argument in the Circuit Court of Appeals for the Seventh Circuit; *Woodward* v. *Commissioner*, 27 B.T.A. 1426, now pending on appeal to the Circuit Court of Appeals for the Second Circuit; *Blow* v. *United States* (N.D.Ill.), decided September 1, 1933, unreported, now pending before argument in the Circuit Court of Appeals for the Seventh Circuit.

arise constantly in the future. A decision by this Court is therefore deemed necessary in order to settle the question with a minimum of expense and delay.

2. The question presented is also of general importance to a large number of taxpayers who have sustained "capital net losses". Section 101 (b) of the Revenue Act of 1928 (*infra*, p. 10) provides that where a taxpayer has sustained a capital net loss, such net loss is to be segregated from ordinary items of net income and the tax is based upon this ordinary net income minus 12½% of capital net loss. It will be noted that this section, where applied, treats capital net losses in the same manner as Section 101 (a) treats capital net gains. In *Elkins* v. *Commissioner*, 24 B.T.A. 572, the Board held that capital net losses should be segregated entirely from ordinary net income and that the allowance for contribution deductions should be computed with reference to the ordinary net income excluding all consideration of capital net losses. This decision was followed in *Livingood* v. *Commissioner*, 25 B.T.A. 585.

The court below noted (R. 28) that the question of proper treatment of capital net losses in determining contribution deductions is identical in principle with the question here involving capital net gains, and that the construction favorable to the taxpayer in this case will operate to the detriment of taxpayers in the case of capital net losses. Consequently, a decision by this Court on the question

here involved will also dispose of the question of proper allowance for contribution deductions in cases of capital net losses.

3. A decision of this Court is also necessary in order to settle the confusion now existing in the administration of the provisions involved. Originally the Bureau of Internal Revenue held that capital net gains and capital net losses should both be included in computing the 15% limitation. I.T. 2104, III-2 Cumulative Bulletin 152. Following the decision of the Board of Tax Appeals in the *Elkins* case, *supra,* the Bureau reversed its ruling, acquiesced in the *Elkins* decision (XI-2 Cumulative Bulletin 3), and held that neither capital gains nor capital losses should be included (Mim. 3931, XI-1 Cumulative Bulletin 33; Mim. 3986, XI-2 Cumulative Bulletin 29; G.C.M. 11324, XI-2 Cumulative Bulletin 267; I.T. 2668, XI-2 Cumulative Bulletin 268). An acceptance of the decision below will leave the matter in further confusion and will necessitate a second reversal by the Bureau. A decision by this Court is requested in order that the question may be settled finally one way or the other.

4. While the decision below is the first decision by any Circuit Court of Appeals on the precise question here presented, the decision apparently conflicts in principle with the decision of the Circuit Court of Appeals for the Fifth Circuit in *Westfeldt* v. *Commissioner,* 63 F. (2d) 882. That case holds that where an individual on a calendar

year basis sustains a capital net loss in 1924 and also reports income from a partnership having a fiscal year ended in 1924, the amount to be placed in the lower brackets of the rate schedule applicable to 1924 under Section 207 (b) of the Revenue Act of 1924 (*infra*, p. 9) is the amount of his ordinary net income undiminished by any part of the capital net loss. The court recognized the principle of segregation invoked by the Commissioner in this case and after discussing the capital net gain and capital net loss provisions of the Act, said (p. 883):

> the capital items thus put under the 12½% flat rate go out of the computation of the taxes under the regular rates, and the "other income" to which partnership gains are to be added is unaffected by the capital items.

Wherefore, it is respectfully submitted that the petition should be granted.

J. CRAWFORD BIGGS,
Solicitor General.

MARCH, 1934.

APPENDIX

Revenue Act of 1924, c. 234, 43 Stat. 253, 261:

SEC. 207. (b) If a fiscal year of a partnership begins in one calendar year and ends in another calendar year, and the law applicable to the second calendar year is different from the law applicable to the first calendar year, then (1) the rates for the calendar year during which such fiscal year begins shall apply to an amount of each partner's share of such partnership net income (determined under the law applicable to such calendar year) equal to the proportion which the part of such fiscal year falling within such calendar year bears to the full fiscal year, and (2) the rates for the calendar year during which such fiscal year ends shall apply to an amount of each partner's share of such partnership net income (determined under the law applicable to such calendar year) equal to the proportion which the part of such fiscal year falling within such calendar year bears to the full fiscal year. In such cases the part of such income subject to the rates in effect for the most recent calendar year shall be added to the other income of the taxpayer subject to such rates and the resulting amount shall be placed in the lower brackets of the rate schedule applicable to such year, and the part of such income subject to the rates in effect for the next preceding calendar year shall be placed in the next higher brackets of the rate schedule applicable to such year.

(U.S.C., Title 26, Sec. 938.)

Revenue Act of 1928, c. 852, 45 Stat. 791, 799, 811:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * *

(n) *Charitable and other contributions.*—In the case of an individual, contributions or gifts made within the taxable year to or for the use of:

* * * * *

(2) any corporation, or trust, or community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes * * *;

* * * * *

to an amount which in all the above cases combined does not exceed 15 per centum of the taxpayer's net income as computed without the benefit of this subsection. * * *.

SEC. 101. CAPITAL NET GAINS AND LOSSES.

(a) *Tax in case of capital net gain.*—In the case of any taxpayer, other than a corporation, who for any taxable year derives a capital net gain (as hereinafter defined in this section), there shall, at the election of the taxpayer, be levied, collected, and paid, in lieu of all other taxes imposed by this title, a tax determined as follows: a partial tax shall first be computed upon the basis of the ordinary net income at the rates and in the manner as if this section had not been enacted and the total tax shall be this amount plus 12½ per centum of the capital net gain.

(b) *Tax in case of capital net loss.*—In the case of any taxpayer, other than a corporation, who for any taxable year sustained a capital net loss (as hereinafter defined in

this section), there shall be levied, collected, and paid, in lieu of all other taxes imposed by this title, a tax determined as follows: a partial tax shall first be computed upon the basis of the ordinary net income at the rates and in the manner as if this section had not been enacted, and the total tax shall be this amount minus 12½ per centum of the capital net loss; but in no case shall the tax of a taxpayer who has sustained a capital net loss be less than the tax computed without regard to the provisions of this section.

(c) *Definitions.*—For the purposes of this title—

(1) "Capital gain" means taxable gain from the sale or exchange of capital assets consummated after December 31, 1921.

(2) "Capital loss" means deductible loss resulting from the sale or exchange of capital assets.

(3) "Capital deductions" means such deductions as are allowed by section 23 for the purpose of computing net income, and are properly allocable to or chargeable against capital assets sold or exchanged during the taxable year.

(4) "Ordinary deductions" means the deductions allowed by section 23 other than capital losses and capital deductions.

(5) "Capital net gain" means the excess of the total amount of capital gain over the sum of (A) the capital deductions and capital losses, plus (B) the amount, if any, by which the ordinary deductions exceed the gross income computed without including capital gains.

(6) "Capital net loss" means the excess of the sum of the capital losses plus the capital deductions over the total amount of capital gain.

(7) "Ordinary net income" means the net income, computed in accordance with the provisions of this title, after excluding all items of capital gain, capital loss, and capital deductions.

(8) "Capital assets" means property held by the taxpayer for more than two years * * *

* * * * *

(d) *Collection and payment of tax.*—The total tax determined under subsection (a) or (b) shall be collected and paid in the same manner, at the same time, and subject to the same provisions of law, including penalties, as other taxes under this title.

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